INTERNATIONAL ISOTOPES INC
Form 10QSB
August 13, 2004

FORM 10-QSB

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended
June 30, 2004

Commission file number:
0-22923

INTERNATIONAL ISOTOPES INC.

(Exact name of registrant as specified in its charter)

Texas	74-2763837
(State of incorporation)	(IRS Employer Identification Number)

4137 Commerce Circle, Idaho Falls, Idaho	83401
(Address of principal executive offices)	(zip code)

208-524-5300

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES [X] NO [ ]

As of August 5, 2004 the number of shares of Common Stock, $.01 par value, outstanding was 159,064,660.

INTERNATIONAL ISOTOPES INC.

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Part I. Financial Statements

Item 1. Financial Statements

INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

Assets	June 30, 2004 (unaudited)	December 31, 2003
Current assets:		
Cash and cash equivalents	$ 752,332	$ 160,216
Accounts receivable	420,785	203,152
Inventories	2,274,558	2,283,752
Prepaids and other current assets	166,181	190,979
Total current assets	3,613,856	2,838,099
Long-term assets		
Restricted certificate of deposit	151,745	150,573
Property, plant and equipment, net	765,836	617,287

Capitalized lease disposal costs, net of accumulated amortization of $41,538 and $35,604 respectively	107,794	113,728
Patents, net of accumulated amortization	97,125	--
Total long-term assets	1,122,500	881,588
Total assets	$ 4,736,356	$ 3,719,687

Liabilities and Stockholders' Equity

Current liabilities		
Accounts payable	$ 302,277	$ 320,554
Accrued liabilities	246,476	150,475
Current installments of notes payable	26,098	756,725
Total current liabilites	574,850	1,227,754
Long-term liabilities		
Obligation for lease disposal costs	149,332	149,332
Notes payable, excluding current installments	2,268,331	898,664
Mandatorily redeemable preferred stock, $0.01 par value; 850 shares outstanding	850,000	850,000
Total long-term liabilities	3,267,663	1,897,996
Stockholders' equity		
Common stock, $0.01 par value; 250,000,000 shares authorized; 159,064,660 and 139,363,046 shares issued and outstanding, respectively	1,590,647	1,393,630
Additional paid-in capital	87,773,530	87,168,957
Retained deficit	(88,470,334)	(87,968,650)
Total stockholders' equity	893,843	593,937
Total liabilities and stockholders' equity	$ 4,736,356	$ 3,719,687

See accompanying notes to condensed consolidated financial statements.

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INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES
Unaudited Condensed Consolidated Statements of Operations

	Three Months ended June 30,		Six Months en
	2004	2003	2004
Sale of product	$ 467,359	$ 785,262	$ 1,210,684

Cost of product	325,780	430,567	768,735
Gross profit	141,579	354,695	441,949
Operating costs and expenses:			
Salaries and contract labor	161,956	110,982	318,690
General, administrative and consulting	266,236	279,872	528,979
Research and development	13,412	10,680	26,979
Total operating expenses	441,604	401,534	874,648
Operating loss	(300,025)	(46,839)	(432,699)
Other income (expense):			
Other income	30	20,867	8,729
Interest income	590	1,402	1,340
Interest expense	(40,792)	(50,281)	(79,055)
Total other expense	(40,172)	(28,012)	(68,986)
Net loss	$ (340,197)	$ (74,851)	$ (501,684)
Net loss per common share - basic and diluted	$ (0.00)	$ (0.00)	$ (0.00)
Weighted average common shares outstanding - basic and diluted	144,684,246	95,572,893	142,372,917

See accompanying notes to condensed consolidated financial statements.

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INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES
Unaudited Condensed Consolidated Statements of Cash Flows

	Six Months ended June 30, 2004	2003
Cash flows from operating activities:		
Net loss	$ (501,684)	$ (333,578)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	88,576	44,159
Loss on disposal of property, plant and equipment	380	--
Changes in operating assets and liabilities:		
Restricted certificate of deposit	(1,172)	--
Accounts receivable	(217,633)	5,111
Prepaids and other assets	24,798	26,845
Inventories	9,194	145,859
Accounts payable and accrued liabilities	123,773	(241,593)

Deferred revenue	--	88,872
Net cash used in operating activities	(473,768)	(264,325)
Cash flows from investing activities:		
Purchase of patents	(105,000)	--
Purchase of property, plant and equipment	(223,696)	(102,913)
Proceeds from sale of assets held for sale	--	262,235
Net cash provided by (used in) investing activites	(328,696)	159,322
Cash flows from financing activities:		
Proceeds from exercise of warrants	801,590	--
Proceeds from issuance of debt	603,950	743,500
Principal payments on notes payable	(10,960)	(255,883)
Net cash provided by financing activities	1,394,580	487,617
Net increase in cash and cash equivalents	592,116	382,614
Cash and cash equivalents at beginning of period	160,216	441,904
Cash and cash equivalents at end of period	$ 752,332	$ 824,518
Supplemental disclosure of cash flow activities:		
Cash paid for interest	$ 33,874	$ 118,183
Supplemental disclosure of noncash transactions:		
Acquisition of equipment for note payable	$ --	$ 17,523
Sale of assets held for sale through assumption of debt	$ --	$ 345,295
Note payable converted from interest payable	$ 46,050	$ --
Renewal/renegotiation of note payable	$ 733,595	$ --

See accompanying notes to condensed consolidated financial statements.

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INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES
Notes to Unaudited Condensed Consolidated Financial Statements

(1) The Company and Basis of Presentation

International Isotopes Inc (the Company) was incorporated in Texas in November 1995. The Company owns 100% of the outstanding common shares of International Isotopes Idaho, Inc. (I4).

Nature of Operations -The Company is a manufacturer of calibration and reference standards for nuclear medicine, offers a selection of radioisotopes (lutetium-177 and iodine-131) and radiochemicals for various applications such as clinical research, supplies cobalt-60 isotope for use in the Leksell Gamma Knife, and provides general radiological measurement capability for processed gemstones. With the exception of cobalt-60, the Company's normal operating cycle is considered to be one year. Due to the time required to produce high specific activity (HSA) cobalt-60, the Company's operating cycle for the cobalt-60 is considered to be three years. All assets expected to be realized in cash or sold during the normal operating cycle of business are classified as current assets. As of June 30, 2004, the Company had 13 full time employees.

Principles of Consolidation - The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary International Isotopes Idaho, Inc. All significant intercompany accounts and transactions have been eliminated in consolidation.

Interim Financial Information - The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments and reclassifications considered necessary for a fair and comparable presentation have been included and are of a normal recurring nature. Operating results for the six-month period ended June 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. The accompanying financial statements should be read in conjunction with the Company's most recent audited financial statements.

Stock-based Compensation Plans - The Company accounts for stock options issued to directors, officers and employees under Accounting Principles Board Opinion No. 25 and related interpretations ("APB 25"). The Company accounts for options and warrants issued to non-employees at their fair value in accordance with SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123").

No compensation cost has been recognized for its stock options in the accompanying consolidated financial statements. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under SFAS No. 123, the Company's net loss applicable to common shareholders would have been increased to the pro forma amounts indicated below for the six months ended June 30, 2004 and 2003:

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	For the Three Months Ended June 30, 2004	June 30, 2003	For the Six Mon June 30, 2004	J
Net loss applicable to common shareholders, as reported	$ (340,197)	$ (74,851)	$ (501,684)	$
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(10,953)	(30,471)	(28,129)	
Pro forma net loss	$ (351,150)	$ (105,322)	$ (529,813)	$

Loss per share, basic and diluted:				
As reported	$ --	$ --	$ --	$
Pro forma	$ --	$ --	$ --	$

(2) Current Developments and Liquidity

Business Condition - Since inception, the Company has suffered substantial losses. During the three and six-month periods ended June 30, 2004 the Company had a loss of $340,197 and $501,684 respectively compared to a loss of $74,851 and $333,578 during the same periods ended June 30, 2003. During the six-month period ended June 30, 2004, the Company's operations used cash of $473,768 in operating activities. During the period ended June 30, 2003, the Company's operations used cash of $264,325. Management expects to generate sufficient cash flows to meet operational needs during the remainder of 2004 through increased sales, financing, and operating capital; however, there is no assurance that these cash flows will occur.

(3) Net Loss Per Common Share - Basic and Diluted

As of June 30, 2004 there were 67,878,692 and 16,000,000 warrants and options outstanding respectively and 850 shares of Series B redeemable convertible preferred stock that were not included in the computation of diluted net loss per common share as their effect would have been anti-dilutive, thereby decreasing the net loss per common share.

(4) Inventories

Inventories consist of the following at June 30, 2004 and December 31, 2003

	June 30, 2004	December 31, 2003
Raw materials	$ 268,265	$ 268,265
Work in progress	2,001,997	2,007,066
Finished goods	4,296	8,421
	$ 2,274,558	$ 2,283,752

(5) Acquisition of license rights

During the six months ended June 30, 2004, the Company completed the purchase of certain assets, patents and intellectual property related to the fluorine extraction process. The patents were acquired for $105,000 and the equipment for $10,000. The patents and equipment will be amortized/depreciated over their estimated useful lives, which are 10 years for the patents and 5 years for the equipment.

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(6) Notes Payable

The Company completed an unsecured note purchase agreement on January 21, 2004 with certain of the Company's principal shareholders and Directors totaling $650,000. This is an unsecured note accruing interest at 6% per year with a maturity date of December 31, 2005. Interest is to be paid on this note on a semi-annual basis and the Company has the option to prepay the principal balance at any time prior to maturity. The principal of the note and any accrued interest is convertible into shares of the Company's common stock at any time at the option of the holder prior to maturity. The conversion price for this conversion option was $0.18 per share, which was the market value of the common stock.

In July 2004, the Company renegotiated the terms of a note with it's bank. The new terms extend the due date of the note to February 1, 2006 and set the interest rate at the bank's prime plus 1% (7.5% at July 1, 2004) at June 30, 2004 the balance outstanding that was renegotiated was $733,595. The Company also renegotiated with the same bank its $250,000 revolving line of credit changing the due date to July 1, 2005 and fixing the interest rate at the bank's prime rate plus 1% (7.5% at July 1, 2004)with a due date of July 1,2005 ($0 outstanding at June 30, 2004). The loans are secured with accounts receivables, inventory and equipment.

(7) Stockholders' Equity and Warrants

During the quarter ended June 30, 2004, 19,701,614 warrants were exercised and exchanged for 19,701,614 shares of the Company's common stock. The Company received $801,590 for the exercise of these warrants.

(8) Commitments and Contingencies

Litigation

During February 2004, a lawsuit was filed by Iso-Science Laboratories, Inc. dba Isotope Products Laboratories in the Superior Court of the State of California for the County of Los Angeles against the Company, the Company's President and CEO, a significant customer of the Company and certain officers of this significant customer. In March 2004, the Company filed a response to the lawsuit in which the Company denied all of the allegations made in the suit. In addition, the Company has filed a counterclaim against Isotopes Products Laboratories on the basis that Isotopes Products Laboratories filed the suit against the Company with the knowledge that it has no basis in law or fact and the lawsuit was calculated to interfere with the Company's contractual arrangements and prospective business between the Company and its customers. On July 29, 2004 the court granted the Company's motion to dismiss all charges against the Company President and CEO, Steve T. Laflin and another officer of Radqual LLC. The Company will continue to vigorously defend itself in the lawsuit; however, an outcome favorable to the Company is not determinable at this time. Should this lawsuit be settled in a manner unfavorable to the Company, the Company could lose its major line of revenues and could be required to make substantial payments to the plaintiff. The Company has a manufacturing agreement in place with this significant customer, which indemnifies the Company and its officers from any loss arising from this suit. However, there is no guarantee that this significant customer can bear the financial burden arising from defending and possible settlement of this lawsuit.

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Dependence on Third Parties

The production of HSA Cobalt is dependent upon the Department of Energy, and its prime-operating contractor, who controls the reactor and laboratory operations. The revenue associated with the sale of HSA Cobalt is largely dependent on General Electric, the Company's sole customer of this product. The gemstone production is tied to an exclusive agreement with Quali Tech Inc. who in turn has contracts with several Gemstone companies, Medical flood source manufacturing is conducted under an exclusive contract with RadQual, LLC. who in turn has agreement in place with several companies for marketing and sales. A loss of any of these customers or vendors could adversely affect operating results by causing a delay in production or a possible loss of sales.

Contingencies

The Company conducts its operations under an operating license from the Nuclear Regulatory Commission ("NRC"). The details of this license determine the scope of permitted operations and amendments are required to either increase the amount of material permitted or change the types of activities conducted within the facility. The Company is required to maintain a funding reserve adequate to address future decommissioning of the facility. An irrevocable, automatic renewable letter of credit against a $151,745 Certificate of Deposit at Texas State Bank has been used to provide this financial assurance.

(9) Subsequent Events

During July 2004 the Company announced the execution of new contracts for production and recycling of various cobalt-60 sources. This announcement coincided with the Nuclear Regulatory Commission (NRC) approval of the Company's licensing for cobalt production and processing operations.

During August 2004, the Company granted 1,500,000 options to a new employee to purchase shares of common stock with an exercise price of $0.17 per share, which was equal to the closing market price of the common stock on the date of grant. These options vest through August 2007 in increments of 25% per year.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Except for historical information contained herein, the following contains forward-looking information that is subject to certain risks and uncertainties. The Company's actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors including those set forth in the "Risk Factors" section included in the Company's Form 10-KSB, filed with the Securities Exchange Commission (SEC) on March 24, 2004 ("Form 10-KSB"). The following discussion should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in the Form 10-KSB.

RESULTS OF OPERATIONS

Three and six month periods ended June 30, 2004 and 2003.

The Company's net loss for the three and six month periods ended June 30, 2004 were $340,197 and $501,684 respectively, as compared to a net loss of $74,851 and $333,578 for the comparable periods of 2003. The increase in net loss is attributable to increased cost of goods sold and operational expense for new products, such as the Fluorine Extraction Process (FEP), launched and being developed during the period.

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Revenues for the three and six month periods ended June 30, 2004 were $467,359 and $1,210,684 respectively, as compared to $785,262 and $1,144,683 for the same periods in 2003; a decrease of $317,903 and an increase of $66,001 or 5.7% respectively. The decrease in revenues for the quarter was attributable to the cyclic nature of cobalt sales that happened to occur in different quarters in

2004 compared to the previous year. The increase in six-month period revenues more accurately reflect the general growth in Company revenues realized through increased sales of some existing products and through the addition of new radiochemcial product. Gross profit for the three and six month periods ended June 30, 2004 was $141,579 and $441,949 respectively, as compared to $354,695 and $503,033 for the same periods in 2003, a decrease of $213,116 and $61,084 respectively. The decrease in gross profit for the three-month period was again attributable to difference in the timing of cobalt sales in the respective periods and production costs for new products. The decrease in gross profit for the six-month period was attributable to increased production cost associated with the start-up of new product sales during the quarter.

Operating expenses were $441,604 and $874,648 respectively for the three and six-month periods ended June 30, 2004 compared to $401,534 and $790,316 for the same periods of 2003. Salaries and contract labor expenses for the three and six month periods ended June 30, 2004 were $161,956 and $318,690 respectively, as compared to $110,982 and $213,752 for the same periods of 2003, an increase of $50,974 and $104,938 respectively. General, administrative and consulting expenses totaled $266,236 and $528,979 respectively for the three and six month periods ended June 30, 2004 as compared to $279,872 and $553,851 for the same periods of 2003, a decrease of $13,636 and $24,872 respectively. The overall increase in operating expense was largely attributable to increased expenditures, such as wages and marketing consultants, associated with development of new products and start-up of the new FEP product division of the Company.

Interest expense for the three and six month period ended June 30, 2004 was $40,792 and $79,055 as compared to $50,281 and $82,199 for the comparable periods in 2003.

Liquidity and Capital Resources

On June 30, 2004 the Company had cash and cash equivalents of $752,332 compared to $160,216 at December 31, 2003. For the six months ended June 30, 2004, operating activities used cash of $473,768, investing activities used cash of $328,696 and financing activities provided cash of $1,394,580. Cash from financing activities consisted primarily of notes provided by several principals and directors and the conversion of warrants to common stock.

The Company has financed its operations since inception primarily by bank loans, sales of accelerator components and excess equipment, its initial public offering, sales of shares of common and preferred stock in private placements to investors, and loans from stockholders and directors.

The Company's future liquidity and capital funding requirements will depend on numerous factors, including, but not limited to contract manufacturing agreements, commercial relationships, technological developments, and certain market factors. The Company still has a significant amount of Series A and B warrants that remain outstanding from the Company's Rights Offering conducted in 2003. Funds from the additional conversion of those warrants should be adequate to pay down certain of the Company's long-term liabilities and to generate additional cash for the acquisition of assets and continued development of the Fluorine Extraction Process (FEP). This should continue to improve the Company's financial strength, debt ratio, and attractiveness to investors or lending institutions.

Although there can be no assurance, the Company expects that revenues will continue to increase. These increased revenues will provide sufficient funds for operations and capital expenditures.

ITEM 3. CONTROLS AND PROCEDURES

(a) The Company maintains controls and procedures designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission. Based upon their evaluation of those controls and procedures performed within 90 days of the filing date of this report, the chief executive officer and the principal financial officer of the Company concluded that the Company's disclosure controls and procedures were adequate.

(b) Changes in internal controls. The Company made no significant changes in its internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation of those controls by the chief executive officer and principal financial officer.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

During February 2004, a lawsuit was filed by Iso-Science Laboratories, Inc. dba Isotope Products Laboratories in the Superior Court of the State of California for the County of Los Angeles against the Company, the Company's President and CEO, a significant customer of the Company and certain officers of this significant customer. In March 2004, the Company filed a response to the lawsuit in which the Company denied all of the allegations made in the suit. In addition, the Company has filed a counterclaim against Isotopes Products Laboratories on the basis that Isotopes Products Laboratories filed the suit against the Company with the knowledge that it has no basis in law or fact and the lawsuit was calculated to interfere with the Company's contractual arrangements and prospective business between the Company and its customers. On July 29, 2004 the court granted the Company's motion to dismiss all charges against the Company President and CEO, Steve T. Laflin and another officer of Radqual LLC. The Company will continue to vigorously defend itself in the lawsuit; however, an outcome favorable to the Company is not determinable at this time.

Item 6. Exhibits and Reports on Form 8-K

Exhibits:

31 Certification by the Chief Executive and Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32 Certification by the Chief Executive and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Reports on Form 8-K:

None

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

International Isotopes Inc.
(Registrant)

By: /s/ Steve T. Laflin
Steve T. Laflin
President and Chief Executive Officer

Date: August 13, 2004